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Retail Food Sector

Guangnan KK Drops Out of Hong Kong Supermarket Scene

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Report Highlights:

The Guangnan KK chain of 34 supermarkets abruptly closed its doors permanently on June 20 without any prior notice. According to a newspaper report, Guangnan KK has lost HK\$145 million so far this year, HK\$500 million in 2000, and has debts of HK\$209 million. A radio report claimed that Guangnan KK owes its suppliers HK\$0.14 billion in unsettled payments. Since the chain has not met its financial obligations, Hong Kong law dictates that it must be put into liquidation; bankruptcy is not an option.

Includes PSD changes: No
Includes Trade Matrix: No
Unscheduled Report
Hong Kong [HK1], HK

The Guangnan KK chain of 34 supermarkets abruptly closed its doors permanently on June 20 without any prior notice. Employees went to work that morning, only to find a note on store gates saying the stores have ceased operations. Five stores that service People's Liberation Army bases will remain open for the near future, but their longer term prospects are not yet clear.

According to a newspaper report, Guangnan KK has lost HK\$145 million so far this year, HK\$500 million in 2000, and has debts of HK\$209 million. A radio report claimed that Guangnan KK owes its suppliers HK\$0.14 billion in unsettled payments. Since the chain has not met its financial obligations, Hong Kong law dictates that it must be put into liquidation; bankruptcy is not an option.

Yip Yuk Chuen, Chairman of the Guangnan Group which owns Guangnan KK, cited several factors for the closure: high rents; inability to expand the number of stores to the critical level for efficient operation; and failure to secure preferential terms from suppliers. The chain signed 5-year store leases in 1996 before the Asian crisis. Since then, property values in Hong Kong have dropped significantly, and during those years Guangnan KK locked itself into high rents set during the pre-crisis property boom. When Guangnan took over KK supermarkets in 1996, the original plan was to open 70-80 stores. In practice, the chain reached only 40 stores, which resulted in higher operating costs and reduced leverage to negotiate favorable terms with suppliers.

Other factors not mentioned by Guangnan's management probably played an equally decisive role in its demise. Some local media claimed that poor, and even corrupt, management prevented Guangnan KK from competing effectively in the marketplace - dozens of Guangnan (Holdings) managers were charged with scams exceeding HK\$1.8 billion in value during 2000. Rumors circulated actively in the Hong Kong press 2 years ago that Guangnan KK's collapse was imminent, but the company seemed to have regained its footing financially. There had also been a rumor in financial circles that Guangnan directors were actively involved in suspicious red chip trading practices in 1997. This time there were no rumors in the media prior to the announcement of closing.

A member of the Hong Kong Department Stores and Commercial Staff General Union commented that mid-sized supermarkets like Guangnan KK are in a particularly tough situation. They are not big enough to obtain competitive pricing from suppliers, but not small and flexible enough to continually offer exciting new product lines in order to grab the consumer's attention.

Guangnan's departure from the Hong Kong supermarket sector left the duopoly of Park 'N Shop and Wellcome with less competition and perhaps less incentive to offer a diverse line of foods and beverages than in recent memory. During the past 15 months, the Hong Kong supermarket industry has witnessed growing concentration with the departure of Market Republic, Seibu's supermarket operations, Carrefour, adM@rt and now Guangnan KK. It is estimated that Park 'n Shop and Wellcome (with stores numbers of 189 and 237, respectively) may be able to raise their collective share of the market from 70%+ to perhaps 80% following Guangnan KK's demise. The significant remaining competition in supermarket and convenience food stores consists of CRC (reportedly 56 stores), DCH Marts (about 35 stores), JUSCO (7 department store supermarkets) and City'Super (2 stores).

Yu-Kee, a no-frills, zero-decoration food retail outfit, has been successful selling locally-sourced budget foods at rock-bottom prices to a large contingent of local shoppers. They have expanded to 50 stores in the last 10 years. Yu-Kee's success may lend credibility to the theory that to survive, Hong Kong retailers must either be large and upscale like Park'n Shop or small and economical like Yu-Kee. Guangnan KK didn't fit into either of these categories.

The impact of Guangnan's closure on U.S. suppliers is unknown at this point. The range of western-style products in Guangnan KK stores was somewhat limited due to the very localized clientele they served, so it anticipated that outstanding payments to U.S. suppliers would be fairly minimal.